

MINUTES
REGULAR MEETING OF THE BOARD OF LAND COMMISSIONERS
Monday, September 19, 2005, at 9:00 a.m.
State Capitol Building, Room 303

PRESENT: Governor Brian Schweitzer, Superintendent of Public Instruction Linda McCulloch, Attorney General Mike McGrath, and Secretary of State Brad Johnson

Via Telephone: State Auditor John Morrison

Motion was made by Ms. McCulloch to approve the minutes from the regularly scheduled meeting of the Board of Land Commissioners held August 15, 2005. Seconded by Mr. McGrath. Motion carried unanimously.

BUSINESS TO BE CONSIDERED

805-4 RECIPROCAL ACCESS AGREEMENT SUMMARY

Mary Sexton, Director, DNRC, said we are bringing this item back to the Board from last month. It is a reciprocal access agreement summary with some additional information. This is with Louisiana Pacific Corporation and Weston Ranches Inc.

David Groeschl, DNRC Forest Management Bureau Chief, said I will cover both reciprocal access agreements together since they are related to each other. He produced a map of the areas and said the first reciprocal access is with Mr. Weston, a rancher. There is a public access road, the department needs 400 feet across Mr. Weston's property to perfect access to the state lands. We currently do not have all lawful purpose access. Mr. Weston is granting us access across his property and we are reciprocating with access to segments in Section 2 for him to access his 80-acre parcel. Also with this access the state is gaining all lawful public access, Mr. Weston has agreed to allow walking public to the state parcels. He has access across Plum Creek lands perfected and we are in the same process, perfecting access in Section 36. That is Weston reciprocal access.

Governor Schweitzer said Mr. Weston has perfected across Plum Creek?

Mr. Groeschl said yes I believe he has. The next piece is from Louisiana Pacific (LP) who has a parcel in Section 6, in Section 2 there are two reciprocals involved, we are granting reciprocal access to LP to this parcel, they have access across Section 36. These are original grant lands so the access has already been granted to LP in the past. This access was never perfected across the BLM lands. So, we are now reciprocating to complete and allow access to the parcel. The next parcel for consideration is the Wallace Creek drainage area and is where we need access across LP into Section 16. LP already has access into this piece, there is a road. The department has a small segment through Plum Creek into Section 16 that it will be perfecting. This is the section that we have a proposed timber sale on in fiscal year 2008 for 2 MMBf. The cost of acquiring the access is a little over \$12,000 for both LP parcels. It is a pretty good investment to ensure we have future access in this parcel for long term management. Both the parcels that LP has do have buy-sell agreements. When you look at the topographic map lines, the parcels are very steep and rocky. There has been a fire in some of the area and most of it is burned. My understanding is it will be sold for recreational purposes.

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 2

Governor Schweitzer asked can you identify any streams on the parcels?

Mr. Groeschl replied I don't believe there are any drainages on these parcels. These are right off I-90, West of Missoula, and it is very steep, rocky, and dry ground.

Ms. Sexton said to reiterate what the excess cost calculation has given the land values and the road costs LP transaction, the state would owe them about \$12,500 and the Weston process is \$646. The department recommends these reciprocal agreements be approved and the authorization for payment.

Motion was made by Mr. Johnson to approve the reciprocal agreement requests. Seconded by Mr. McGrath. Motion carried unanimously.

905-1 BLUE EYED NELLIE WMA ACQUISITION - FWP

Deb Dils, FWP Land Section Supervisor, said I'm here to request approval of the 97-acre acquisition West of Anaconda. The land is owned by Howard and Joanne Long of Missoula, and the cost would be \$300,000; \$270,000 of that would be paid by FWP through the license auction account for Big Horn sheep and \$30,000 is being paid by the North American Wild Sheep Foundation and the Anaconda Sportsmen's Club. This particular land is heavily used during the winter, the sheep cross back and forth to get to water and they have been expanding into the Garrity Mountain area. Because of the development going on nearby we would like to secure this so there will continue to be that corridor. The FWP Commission approved the acquisition on September 8th after going through a MEPA process and a public hearing. We have had total support, no negative comments were received. FWP requests the Board's permission to move ahead with the acquisition.

Mr. McGrath said by way of information, the Garrity Mountain WMA is an area where we did a big exchange a couple of years ago through the NRD program with the Rocky Mountain Elk Foundation, Y-P Timber and the Forest Service. So this actually fits in with a lot of what we did a few years ago in that area.

Motion was made by Mr. McGrath to approve the Blue Eyed Nellie acquisition. Seconded by Ms. McCulloch. Motion carried unanimously.

905-2 SHEEP GAP TIMBER SALE

Ms. Sexton said this timber sale is about 5.5 miles from Plains, in Sanders County. The estimated volume is 28,000 tons with a minimum value of \$602,000. The sale area is 454 acres and the proposed treatment includes shelter wood, variable retention harvest, commercial thinning, and rights-of-way of 30 acres. Ponderosa Pine and western larch are the favored leave tree species to mimic historical conditions. In this harvest request 58% will be with tractor, 42% skyline. There will be new roads constructed totaling 3.14 miles. All roads will be obliterated after the sale. There was a public input process and several issues surfaced including road access (all will be closed and seeded upon completion of the sale); wildlife (habitat for the Flammulated owl and Pileated woodpecker will be favored with retention of Ponderosa pine and western larch); public access will be restricted to reduce the potential loss of snags to firewood gathering; roads will be seeded and spot treated for weeds; and for visual impact and aesthetic value

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 3

skyline logging will be used to reduce the visual impacts. There are no old growth stands in the proposed sale area.

Ms. McCulloch asked do we know how much of state land was burned this summer? Or is that something you will evaluate later on?

Mr. Groeschl said that is an assessment that we will give later on when we look at fire season.

Motion was made by Ms. McCulloch to approve the Sheep Gap Timber Sale. Seconded by Mr. Johnson. Motion carried unanimously.

905-3 OIL AND GAS LEASE SALE (Held September 7, 2005)

Ms. Sexton said this sale was held on September 7th and it was another very successful sale totaling \$3.6 million, 205 tracts were sold covering 89,000 acres. The average bid per acre was \$40, and there was a high bid of \$4,000 per acre which unfortunately was a DOT tract not a state land tract. The report was there was no perceived loss due to the change in royalty, bidding was brisk and enthusiastic. I will also add that in the last year oil, and gas production in Montana is up 20-25%. I request approval of the oil and gas lease sale.

Governor Schweitzer said I'd like to say after the Board made the decision to raise the royalty rate from 1/8 to 1/6, I received a few e-mails and certainly while I was in Billings I had people discuss this with me in public places. Most of the people concerned were sure this would have a chilling effect on development of oil and gas in Montana. So if there is a chill, I think it is room temperature.

Mr. Johnson said how many of these tracts have a production record and how many are being wildcatted?

Monte Mason, DNRC Minerals Management Bureau Chief, said I'd say virtually all except one is unproductive. One had an existing well on it. These have been leased before, and are being leased again. But there is no development on them to date.

Mr. Morrison said this is the largest lease sale we've had by some margin, correct?

Mr. Mason said fairly high, yes. Its #6 on our top sales of all times as far as total revenue brought in. As far as average bid per acre, it is #2. The #1 was a couple of sales ago when we also had a very nice sale. The high there was \$42 per acre roughly, and this one was \$40 per acre.

Governor Schweitzer said I would just suggest the Board keep an eye on this. Mary, continue to inform us as to how these sales are going. When we made this decision I think it was pretty clear that if we saw an adverse effect, if we saw declining oil and gas activity, and declining revenues that we would reinvestigate it and I am sure the Board would be more than happy to do that.

Motion was made by Mr. McGrath to approve the September 7th oil and gas lease sale. Seconded by Ms. McCulloch. Motion carried unanimously.

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 4

905-4 COMMUNITIZATION AGREEMENT (Burlington Resources)

Ms. Sexton said this communitization agreement is located in Richland County with Burlington Resources. This is a spacing unit of 1280 acres of which the state owns 640, half the unit. Production will be allocated to each tract based on the relationship of the acreage to the total. The department will receive 6.5% of all oil and gas production. Again, this will be at the old royalty rate because that's when this lease was originally let.

Motion was made by Mr. Johnson to approve the communitization agreement. Seconded by Mr. McGrath. Motion carried unanimously.

905-5 SET MINIMUM BID AMOUNT FOR LAND BANKING PARCEL

Ms. Sexton said this is a request for setting a minimum bid for a land banking parcel. This parcel is what we call #202 Haskell Mountain in Flathead County. It is an 80-acre parcel near Kalispell, a remnant of Section 36, and was not homesteaded at statehood. Currently there is not legal access although there is access through the Forest Service. This is a DNRC-nominated parcel and has had very low activity on it, there was a timber sale on it in the 1940s, it is fairly steep. The appraisal was done by the department and it recommends a minimum bid of \$189,360, that is \$2,367 per acre. This parcel is next to Forest Service land. This has come before the Board before, this is the second time which is to set the minimum bid.

Motion was made by Ms. McCulloch to approve setting a minimum bid for parcel #202 Haskell Mountain. Seconded by Mr. McGrath. Motion carried unanimously.

905-6 WHITEFISH NEIGHBORHOOD PLAN PROPOSAL PROCESS

Ms. Sexton said this item is for approval of the proponent-propelled proposal process for the Whitefish Neighborhood Plan. We have had some proposals come forward regarding the Whitefish Plan and we determined that it is necessary to have a clear process that we utilize when proposals come forward. I met recently with representatives of the Whitefish community, legislators, the mayor and others from the community regarding their interest in realizing elements of the Whitefish Plan. With this is a fairly straightforward process. First there is a Letter of Interest by a proponent of a proposal, and incidentally next month you will have a proposal from the City of Whitefish and other entities that are collaborating on a larger proposal for addressing the plan; after the Letter of Interest we may require a pre-application form for specific information. Once we've received that we will meet with the proponent. We will then produce a staff report that includes our conclusions, it goes through the Record of Decision, that is the Programmatic EIS funnel process, we look at transaction options be they lease, sale, easement or whatever they might be, and we look at possible transaction partners. The objective here is to try and encourage partners to work together as much as possible with these proposals. Following the staff report we issue a coordination notice to make sure every entity in the area that may be interested in this proposal is informed. This is before any MEPA process takes place. Based upon the response from the public notice and public input we assemble an Initiation Agreement which identifies rural government or other transaction partners, it talks about appraisal instructions, sequence and timeframes, as well as public involvement, and of course the execution phase which is where the process or whatever transaction type it might be, a sale, an easement, or an exchange, would be spelled out and the MEPA process would be completed. Again, all exchanges, sales, easements, or leases that are over \$50,000 would be approved by

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 5

the Land Board. So, this is a process we are going through and again next month we will probably start testing this as the City of Whitefish will come forward with a Letter of Interest. Ms. Sexton requested approval for the process.

Mr. Morrison said it is my understanding that this four-phase approach has been vetted with some of the folks who have been involved in the planning process in Whitefish.

Ms. Sexton said that's correct. We have had a meeting and sent them various draft copies. This is just a process proposal so it is clear to those proposal proponents out there what kind of process we will be following. But yes, its had a good deal of public review.

Motion was made by Mr. Morrison to adopt the Whitefish Neighborhood Plan proposal process. Seconded by Ms. McCulloch. Motion carried unanimously.

905-7 RIGHTS-OF-WAY APPLICATIONS

Ms. Sexton said you might look at the first page of the rights-of-way application requests because we have introduced a summary sheet so it is more clear how the rights-of-way are divided out according to types of applications. We have historic telephone lines from Triangle Telephone, #11943, #12199, #12200 through 12202, #13105 through 13123; Historic electric lines from both Sheridan Electric Coop, #12806 through 12810, and from Sun River Electric, #13040 through 13047, #13066 through 13070, #13073, and #13097 through 13103; Historic county roads, these are the two that are being brought back again regarding historic right-of-ways, from Prairie County, #13513 through 13116, and from Fallon County, #13129 through 13130, and #13428 through 13431; Historic private roads from Leroy "Jack" Bergum, #13595; Bridge easements for easements across navigable waterways from the Department of Transportation, #13594, and from Daniel G. Beltram, #13596; New install – telephone utility from Range Telephone Cooperative, #13597 through 13601; and one for a Fire Hall from the City of Kalispell, #13546. If you'll recall a couple of months ago they were here regarding the increase in the easement cost because the footprint of their fire station increased. That has now been reduced so it has come in line with their funding opportunities. They are getting credit for the sewer and water which is running through their footprint, and I think they are very pleased with this change in their easement. Also, Harold Blattie from the Montana Association of Counties is here today to speak to the historic county road requests, and there is an informational item concerning county roads and historic rights-of-way for discussion later.

Mr. Johnson asked if it would be permissible for the Board to segregate out the Prairie and Fallon Counties rights-of-way applications until after they have heard the informational presentation on those?

Governor Schweitzer said I think that is appropriate. We can segregate those.

Ms. McCulloch said she wanted to thank the department for the new format for the rights-of-ways. It makes it much easier to find them without flipping through the requests during the discussion.

Mr. McGrath said I don't know if there is anyone from the Department of Transportation here, but the last couple of years we've had these problems with the rights-of-way for bridges with agreements with counties, and then fishing access gets denied after they build a new bridge. I understand there have been a lot of changes in that area. Do you have any information on that? Is anybody here from DOT?

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 6

Mr. Schultz said my understanding is that this site does currently have a fishing access site and public access to this site through the bridge.

Mr. McGrath said of this particular one?

Mr. Schultz said yes, this one.

Governor Schweitzer said this would grant them for forestry and agriculture purposes and not for subdivision or is it segregated?

Mr. Schultz said this one is for MDOT and for the department road access and public use. There is fishing access there and this would allow continued access for the public.

Ms. Sexton said this is the old steel bridge which is approximately two miles East of Kalispell and it is for replacing the existing bridge which doesn't accommodate two travel lanes, it is unsafe. The new bridge would allow two twelve-foot wide travel lanes and two four-foot wide shoulders. A previous easement had been granted for the structure and these were grandfathered in before we had the jurisdiction with our easements for bridges.

Ms. McCulloch said am I correct to understand the proceeds from bridge easements actually goes to the general fund and not to the state land fund?

Mr. Schultz said yes that is the case.

Motion was made by Mr. McGrath to approve the rights-of-way applications with the exception of those from Prairie and Fallon Counties. Seconded by Mr. Johnson. Motion carried unanimously.

INFORMATION ITEMS

805-5 CASH LEASING ON AGRICULTURAL LANDS

Ms. Sexton said in this informational item we covered two requests that came from the Board. First of all, information on cash leasing and then also a legal assessment regarding implementation of cash leasing if the Board so chooses. Regarding the information, we currently have 425,000 acres of crop land in state land and 143,000 of them are enrolled with CRP program. The average income from these lands over the past five years has been \$14.95 per acre. By comparison the five-year average dry land cash lease rate report form by Montana ag and statistics is \$18.24 per acre. So if this rate would apply to all crop and hay land they would generate \$7.7 million per year, or an additional \$1.4 million annually if we were all on a cash lease rather than a crop share.

Mr. Schultz said under a crop share basis we have to verify reporting. Sometimes we have it done by helicopter or sometimes we check reports that are turned in when crops are sold. Under a cash lease scenario that goes away. Whether somebody reports accurately or under-reports, that no longer becomes an issue. The value of that is not included in this revenue potential string. There are potential other revenues to come. Theoretically, if folks are over-reporting or under-reporting in the field now, that would go away and we would also be out of the farm program.

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 7

Ms. Sexton said attached to this document is a legal opinion by Mark Phares, one of our staff attorneys, regarding how this might be implemented. And as to some legal questions there is a bit of a grey area. The question was, may the DNRC pursuant to Mont. Code §77-6-501 require cash leases as opposed to crop share leases on agricultural leases. The short answer is the Board may not require all ag leases be issued in a cash basis but the Board may, consistent with the provisions of the code, issue cash leases. There is a legal analysis here and Mr. Phares is available to answer any questions. Through rulemaking this could be applied administratively although somewhat open to challenges. We look at the conclusion and it is clear that this prohibits the Board/DNRC from requiring all leases be in issued on a cash basis but the sole exception to the general rule is when pursuant to Section 2, "another basis for lease is in the best interest of the state or when a lessee has made substantial improvements for irrigation purposes." I think the language "in the best interest of the state" could be construed and utilized through the rulemaking process for conversion to cash leasing. The other option and perhaps safer is the Board request the department put together a legislative package regarding cash leasing.

Governor Schweitzer said have any of the constituency groups, the farm groups, weighed in on this possibility?

Ms. Sexton said I know most recently I was at a WETA meeting and the Farm Bureau did express support for this. It did not in the past. I think the greatest concern, obviously, comes from Daniels County where about 1/3 of the county is state land. But the Farm Bureau expressed support for cash leasing. And MonTRUST has been very supportive of cash leasing.

Mr. Johnson said the input I have received both from the Montana Farm Bureau and the grain growers is very positive with the caveat that we use real world county production figures in order to establish the cash lease rates. But if we do that, which of course I would assume is the approach we would want to take, we would have some pretty solid support.

Governor Schweitzer said there are two more issues. We have talked about an additional \$1.5 million worth of revenue, and on the cost side we talked about spot checking, but there is more. Because when you are on a crop share basis in the spring of the year the producer is expected to fill out some forms and send them to the department telling them what they intend to plant. After they sign the stuff up at the county office, they send another document in. There is another document they have to sign and it has to be signed off on that they have crop insurance and its been taken care of. Then there is another document in the fall of the year that you send in that tells what your yield is worth. There is a fair bit of FTEs that are involved in this process. When you walk into an FSA office they are hanging around there because they have to go through paperwork and see who has signed up for what, whether it is accurate, and whether there have been any transactions or sub-leasing. So, there is a lot of human resources we are expending on this crop share basis. There is another item. Assuming that every bushel produced on state land is reported, and we are going to make that assumption, most of that wheat is marketed as quick as it is harvested. A producer has no reason to store state grain in his own bin. So if there are any limits in storage or anything else, the first grain that goes to town is the wheat that is owned by the state and that is historically the absolute worst time to sell. There is a low market for that, there is a shortage of rail cars, there is an anti-incentive to market at that time. So the State of Montana, with all of its marketing capabilities and whole departments of commerce and agriculture, sell its wheat at the worst possible time. Now, we've got some business people that are in government and virtually every one of them knows it is the wrong time to sell. But it's out of our hands. So, if we go to a cash lease I think the State of Montana would get substantially more than what we've even described here. We have some opportunities of some

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 8

farmers and competitive bids stepping up and finding that market value. It starts with finding actual market value but as time goes on there will be bids out there that would move this to a marketplace.

Mr. Johnson said the only thing I would add is, going back and putting on my former county extension agent hat, we never counseled landowners to enter into share basis. Never. It was almost a policy and I think it is good business for us to try and make this transition.

Governor Schweitzer said while I agree it is good business, it may mean there will be a limited number of trips to Scobey by members of the Land Board for a few years because the word I hear from folks, in particular in Daniels County, they don't support this. But it is interesting because they are also very active in the grain growers and the Farm Bureau which are supporting it. I guess the question here is, we really have two options before us. One is to work towards a piece of legislation that we take to the legislature or something we might do through rulemaking. Is there any thought on that?

Mr. McGrath said based on the memorandum we have it is pretty clear that we do need to ask the legislature to amend the statute. It sounds like we would get pretty good support for that and it seems to me that we ought to ask the staff to work on that as part of the legislative package going into the next session.

Ms. Sexton said would you like me to place this on the agenda next month as an action item so the Board can officially request that? Or is this something at this point in time you would like to ask the department to put together as a legislative package?

Mr. McGrath said at some point the Board is going to have to approve a legislative package so we don't necessarily have to do it next month. But at some point you will need to bring it to the Board.

Ms. Sexton said so my understanding is, the preference is to look at a legislative package rather than administrative rules working with the current statute.

Mr. McGrath said yes.

805-6 COUNTY ROADS AND HISTORIC RIGHTS-OF-WAY

Jeanne Holmgren, DNRC Real Estate Management Bureau Chief, said the Board has an information packet that provides it with supporting documentation with regards to Lassen v. Arizona in that the disposition of trust lands for any purposes, even rights-of-ways, has to be compensable to the state in which the rights are being granted across trust lands. We've gone through a history of the processes to granting an easement especially for county roads. We had originally, over time through the legislature and through the MonTRUST lawsuit, been challenged with our ability to grant access to county roads at less than fair market value. We were sued over that and we lost. Subsequently in the 2001 legislature we came back with legislation for historic rights-of-ways. Easement standards are waived for county roads that come under historic rights-of-way, and for utilities that already have existing metes and bounds surveyed for that road. As for the MEPA process, that is waived since the activity is already existent on trust land. So, that provides an avenue for counties and utility companies to come forward and pay fair market value for those roads. One of the reasons counties are being encouraged by some of the landowners in their county to perfect this is that through their disposition, the private disposition of their holdings, when a county road is not fully legitimized especially over state trust lands, there is a cloud on

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 9

their title. That is another impetus for the counties to come forward and perfect their easements on trust lands. Some of the things that we have been doing is working with the MACO, going to their regional meetings, and discussing with those folks our process, how we are trying to make it as clean and user-friendly as we can. We've also encouraged them along with utility companies, as utility companies typically lie within county roads, to come together and acquire one easement. Therefore we are not issuing two easements to two separate entities. That is how we've gotten to where we are today. Through Lassen v. Arizona, through legislation, and through our ability to not issue an easement at less than fair market value, to today in issuing easements at fair market value but reducing some of the standards because the road is already existing, the impacts are already there, reducing those survey standards.

Ms. Sexton said I would note also that the sunset has been extended by the legislature. It was set to sunset October 1, 2006 and it was extended through October 1, 2011, to give counties a little bit more time. Again, that is with the caveat that they don't have to do a survey and that is really a reduced workload for counties in order to complete this.

Ms. Holmgren said this statute does not require them to obtain an easement. We are not going out and enforcing and requiring counties to come forward and perfect all of their easements on trust lands. This gives them a window to come under the statute as Director Sexton described, they do not have to pay for a survey and go through some of the other processes that we have.

Mr. Johnson said my understanding is from this presentation, we simply don't have alternatives here as a Board.

Harold Blattie, Montana Association of Counties (MACO), said I am sure the county commissioners across the state would be quite ecstatic if someone were to find a different way to skin this cat. I have to tell you that Lisa Axline and Jeanne Holmgren have been very patient with county commissioners and this lease. As Jeanne mentioned, attending our district meetings on several occasions, telling the counties about the process and informing them of the benefits of doing it in a timely manner. Needless to say, it is something that was certainly not embraced early on. I believe as the level of understanding and just more information regarding the resulting litigation made clear that counties are going to have pay for these rights-of-ways, there has been a greater level of acceptance. The recommendation we have made to the counties is to go out and do a good on-the-ground inventory, an inventory where you have county roads crossing school trust lands. And determine do we need an access through there? Is there a right-of-way beyond there? If it is going through a school section that simply accesses additional public lands, the county really doesn't have an interest in having that right-of-way because the public will always have that access across there. But conducting a very good inventory. I can tell you that Flathead County has estimated their cost to be over one million dollars, in other counties it ranges from very little. Interestingly enough, Daniels County it is hardly any because they have already acquired rights-of-ways. So it is different for every county. The legislation that extended the sunset was at our request because it will let the counties move ahead but it will spread their payments out rather than having to pay for it all at once. It took us a long time to get to an acceptance and there was a grudge against acceptance but I believe for the most part counties do understand there is a great benefit to doing it now because the cost of being able to use good documental evidence as to the existence of those rights-of-way roads actually being there is going to be significantly cheaper than having to go back do a survey. There is a significant financial benefit for the counties to go ahead and move through the process as it is currently laid out.

Mr. Johnson said it seems to me on the one hand the court tells us that we cannot delegate our authority with regard to preference, then it turns around and tells us we have no authority with regard to this kind of

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 10

management decision. I think it is patently absurd that this Board does not have the authority to enter into this kind of mutually beneficial agreement with other government entities.

Governor Schweitzer said any comments about that? Mr. Attorney General?

Mr. McGrath said no.

Motion was made by Mr. McGrath to approve the rights-of-way applications by Fallon and Prairie Counties. Seconded by Ms. McCulloch. Motion carried unanimously.

905-8 QUORUM FOR LAND BOARD

Ms. Sexton said this came up in the July meeting when we only had three Land Board members present. This caused quite the stir among our legal people. Thank you to Candy West, Tommy Butler, and others who reviewed this. It is not absolutely clear in statute so I know that Candy went back and looked some of the Constitutional Convention transcripts where we do not have agreement over whether the code pertained to votes by executive agencies apply but I don't think it matters since we all agree the Constitutional Convention transcripts settle the question which requires "a majority of three for a decision would emphasize the principle of caution over that of expediency." Therefore, if there are only three Land Board members present then all three have to agree on an issue for that to be finally concluded. Again, this is taken from the transcripts of the Constitutional Convention. So, I think this question has been decided.

Governor Schweitzer said fortunately it seems this Land Board agrees on a unanimous basis about 90% but it is great to know.

Ms. Sexton said unusual circumstances came up and now we have some clarification. We have to ask, however, we are going to look into the issue for the next meeting whether the deputy of a Land Board member can actually be a voting member and that would be when the member is absent. We will be asking for a legal analysis of that and have an information item next time.

905-9 RETAIN RATHER THAN SELL RESIDENTIAL LEASE PREFERENCE

Ms. Sexton said this item is in response to public information from our last meeting, the family from Gallatin County. And this refers to the retention rather than the sale of residential lease preferences.

Ms. Holmgren said actually going back through this and having staff put together information it brought back memories as I was involved in the beginning. In 1989 the legislature passed a law that allowed our cabin and homesite lessees to bring forward an application to purchase their leases. That allowed a 10-year window for all cabin and homesite lessees and allowed an additional 10-year window for those that were senior citizens or handicapped. In 1991 we consummated rules by which we would sell those cabins and homesites. Through the course of a couple of years since the advent of the administrative rules process, we brought cabin and homesite sales before the Board. The Board at that time postponed any decision associated with the sale of those cabin and homesites and directed us to work with staff. We created a working group and essentially came up with a couple of methods. In looking at a 60-year window a "keep versus sale" what would it mean for us revenue-wise, the appreciation of the value over

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 11

60 years versus selling the property. As the cabin and homesites appraised value of those lands appreciate we are now at a lease rate of 5% rather than 3.5%. It showed financially that it was in the best interest of the trust to retain those properties rather than sell them. The second method was that in the event we were to consider the sale of any of those homesite properties the value we would start the minimum bid at would be the value of the department keeping it over a 60-year period. That is what we would sell it at. We did sell one cabin and homesite, the minimum at that time was \$3,000 over 60 years, it was \$33,000, and we did sell it to that gentleman for that higher value. Throughout the course of the process of the ability to sell our cabin and homesites under the cabin site sale process, the Board directed us and adopted a "no sale" policy. Under land banking, because we were generating a rate of return of 5%, that was put into the category of those folks that were questioning for the sale of their cabin and homesite, but we were generating a revenue off of those that we did not wish to dispose of at that time. Some of the questions from the last Land Board that were asked were did the Bates' make an application to buy their cabin or homesite? And the answer was no. Secondly, what are some of the options available for them in exchange? Mr. McGrath asked the question about the Mandeville's. For Mandeville it was a five-acre homesite. We did a land exchange of some adjacent property to them. In that situation we did dispose of a homesite but we did a land exchange and we got 17 acres for the five acres. That gives the Board an overview, the history as to where we are today. We have statutes that were passed, we went through rulemaking, established a policy with the Land Board, and we are now at land banking. We have not been favorable as far as selling those because of the rate of return we are obtaining.

Mr. Johnson said as I understand this situation, it is fairly unique in that this originally was deeded land owned by this family. Ownership moved to the state in lieu of payment of taxes. Is that an accurate understanding?

Governor Schweitzer said I think that is the description we received from the family that came before us.

Mr. Johnson said if, in fact, that is the case, I think we need to seriously consider an exemption of the policy. I would be the first one here to say if they had been a lessee through the entire history of this story that the policy is sound and we should stay with that. But for the state to take private property when somebody is in hard times, they stay on the land, they work hard, they get well financially, and we tell them we are not going to let them buy their property back. I think it is just fundamentally wrong. And I would hope we'd exercise, I understand the consistency in applying policy is important, but it is also important for this Board to exercise judgment from time to time when we have unique situations. And I think this one is.

Ms. Holmgren said we did do some research. This is a Section 16. This was a section that came to the state at statehood and through our research we believe that some of the adjacent land the lessee owned was something that they subsequently lost through taxes. But this was not a parcel that they had owned and then lost. This came to the state at statehood.

Mr. Schultz said we can look at anything the Board wants us to look at and reevaluate things. The only comment to be aware of is when land is sold it has to go to oral auction. So even though these folks live there right now, if they want to make nomination for us to sell this tract under land banking or any other sale process, it would go out for open competitive bid for the sale. This property is near Manhattan and I don't know the environment there in terms for competing bids, but it is possible that the best scenario for them retaining the property would be to retain the lease as opposed to trying to purchase it in the open market.

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 12

Ms. Sexton said if the Board would like to entertain some action on this item, we can certainly present it as an action item at the coming Land Board meeting.

Governor Schweitzer said in lieu of the idea that this piece of property has belonged to the state for a long period of time, since the time it was initially granted to us, and it doesn't appear that under that circumstance as described that would be a place certainly to look at changing our view of that land ownership and give them an opportunity. But even under the circumstance, would it mean that this farm family would have to go out on the competitive market and, probably in Manhattan, somebody with more money than the person who farms it could step in and bid that higher than the value to them as a farm house?

Mr. Schultz said yes that is probably the case. However, the statute does allow for preference, they could match the high bid. But it depends upon how high the bid went, so there is a lessee preference to match the high bid.

Governor Schweitzer said does this family understand the things you just described to us? That that piece of land has actually been leased? Sometimes oral tradition is different than the written tradition. And secondly, that it would go to competitive bid?

Mr. Schultz said I'm not sure they know all that. When they were here they testified that they didn't get the best support from the local office that they couldn't get in touch. We will make contact with them again and let them know the process and other options if they want to propose an exchange. If they do want to propose a sale under land banking we could look at that. But again, explain the reality of the uncertainty if they go through any one of these processes. Land exchange is a more certain option.

Ms. Sexton said I'll make sure they get an explanatory letter, and I can copy you that in your packet of information, so it is well explained to the family.

905-10 PINNACLE GAS RESOURCES COAL BED NATURAL GAS PLAN OF DEVELOPMENT

Ms. Sexton said this was included at my request. This is an EIS we are currently completing from Pinnacle Gas Resources CBNG Plan of Development. This is a little bit different than what we've seen before in that the water will not be discharged into the Tongue River as was the case with Fidelity wells. It will be put into holding ponds for evaporation. This is just for the Board's information we are going through an EIS.

Mr. Mason said we are doing an EA tying off what the Board of Oil and Gas has already done. And it is similar to what the Board has seen before in that there is a state section as part of the overall Plan of Development (POD) but it has been a while since we've been before the Board. We have had a number of PODs in the past with Fidelity, then there were two Fidelity ones that did not involve state lands that took place, there were two Pinnacle ones that did not involve state lands. So it has been a few months. We are bringing this information to you as an informational item. We have done our EA and it is on the street for public comment, our plan would be to bring it back to the Board next month for action.

Bobbi Jo Coughlin, DNRC petroleum engineer, said we are bringing this forward today because the water management issues are a little bit different than what we've seen from Fidelity in the past. A brief history,

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 13

we went through this in significant detail at our last meeting. Coalbed natural gas development in Montana historically Fidelity has their initial 253 wells, there are Badger Hills POD, Dry Creek, Coal Creek which is what we brought before the Board at the last meeting, Pond Creek and Deer Creek we actually do not have land in. Then Pinnacle Gas has presented their Coal Creek POD which did not include state lands, and now the Dietz POD which is what we are presenting today. Inside the CX Field Boundary everything has been developed by Fidelity. Pinnacle has done the Coal Creek POD which is to the northwest of the Dietz and the Dietz is actually what we have now with one section of state land. A total 161 wells, 24 state wells. The Montana Board of Oil and Gas Conservation issued an ROD for all 161 wells on September 6, 2005. We actually tiered ours off of their EA. A total of four evaporation pits on state land and we are requiring all of them be lined, they are all off channel. They have four evaporators proposed in each of their evaporation pits and they are actually going to install them into the pit to minimize the impact they have to the soil and vegetation around them. We have one storage pond proposed on state land. It is also lined and off channel and will be used primarily during the winter months when the evaporation isn't sufficient. Ms. Coughlin showed slides of the off-channel containment pond and a picture of what the evaporators look like.

Mr. McGrath said what is the current use of our section now? Do we have ag leases? Grazing leases?

Ms. Coughlin said we do. There is a grazing lease on our section.

Mr. McGrath said how will that be affected or will that be part of the review?

Ms. Coughlin said they have been contacted by Pinnacle and they are finding a place to put stock watering development for them and they actually have no objections to the project.

Mr. McGrath asked do they propose to use some of this water as stock water?

Ms. Coughlin said yes they do. They will actually run it around the evaporation storage pond.

Governor Schweitzer said it seems to me as time goes forward there are more and more common sense solutions toward treating the water or finding a way of doing coal bed methane resin and this one seems to be common sense. This is water treatment in the cheapest way. We're not using the resin process, we're not using the river as osmosis, we're simply evaporating the water containing 100% of the salts and the presumption is that they will find some mechanical way of removing those salts and placing them someplace in the future.

Ms. Coughlin said they have a pilot project within the Coal Creek project where they are doing a water treatment program. But it is still in the preliminary phase. They are hoping they can expand that if it is sufficient to do that.

Governor Schweitzer said this is water treatment. This particular evaporating the water and collecting the salt.

Ms. Coughlin said right. The salt will stay in the lined pit.

Governor Schweitzer said and then what will be the disposition of the salt that is in the pit?

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 14

Ms. Coughlin said they would actually just fold them into the liner. I am not sure what their exact proposal is for that but it is under the regulatory authority of the Board of Oil and Gas Conservation. They would have to abide by their rules just as they would for any other pit.

Governor Schweitzer said so, they would fold the plastic over, or rubber whatever it is, and then push dirt on top of it and it would be maintained?

Mr. Mason said obviously there is that choice or removing the liner and the soil beneath it. That would be determined at that time at the end judging and looking at what's there, how much, whether we could cap it with topsoil, whether we need to place a clay liner on top of it then topsoil. There are a number of options we can use at that point which is 15-20 years down the road. There are monitoring wells, so we will have information with which to make that decision.

Governor Schweitzer said have we heard any kind of numbers, what their cost of this treatment would be in terms of cost per mcf gas? Are there any estimates? We've heard that the resin process might cost as much as 50 cents an mcf or slightly more to remove the sodium. Is this less expensive?

Mr. Mason said I do not have specific figures but yes I am sure it is, significantly cheaper. But as Ms. Coughlin mentioned, there is a pilot treatment project up north and that is a very small volume right now. We can talk to Pinnacle and see what their expectations are on that but I imagine they will say it is preliminary until they see how this pilot project works as far as efficiency and actual cost. We can sure find out what we can and get back to you.

Mr. McGrath said will there be a bonding requirement for reclaiming the site or is that done through the Board of Oil and Gas? How does that work?

Mr. Mason said the bonding is with the Board of Oil and Gas. By statute we do not have the authority to bond on oil and gas leasing. That was many years ago when the thinking was it is double bonding and in many respects it is. So those areas are bonded at the Board of Oil and Gas and as Ms. Coughlin said they would have to be copasetic with the reclamation as well.

PUBLIC COMMENT:

Suzanne Taylor, Brennan's Wave Project, said this project is on the agenda for the next session in October so I don't want to take too much of your time here but just wanted to give you a preview of things to come. Basically what is happening is there is an existing structure in the Clark Fork River that is in downtown Missoula and a group of private citizens has formed and formed a non-profit entity which is called Brennan's Wave. The objective of Brennan's Wave is to take the existing structure which is known by all to be a safety hazard and upgrade it to not only perform its function as an irrigation structure but also to use it as a recreational structure which is known as a play wave. The way the play wave is created is instead of using concrete and rebar type material which is currently in the river it would use rock features, natural rocks and boulders and create a safe structure that would also allow a bit of a wave there where boaters could play on it. That is a general overview and we'll look forward to educating members of the Board further on this project. At this point we have received a 310 permit from the county and our next step is working through some issues with DNRC. Right now what we're getting are some numbers that are going to be prohibitive for this project. Just to give you an idea, the cost of actually constructing the project is \$300,000. The DNRC issues we need to work through are first of all an easement and the

MINUTES
September 19, 2005
BOARD OF LAND COMMISSIONERS
Page 15

estimates that we're getting currently are the easement will cost \$210,000. In addition, there will be an annual fee of \$21,000 assessed to the project and currently there is a request for liability insurance. At this point we're not here to give a full overview of our opinions but wanted to give the Board a heads-up we're coming your way and that we are looking for ways to work for relief to some of these costs. We think that there are provisions in statute and in addition there are some Board precedents that would come to that end so we could find a way for that project to happen. Right now if those are the costs that are going to be assessed then the project will not occur.

Motion was made by Mr. McGrath to adjourn. Seconded by Ms. McCulloch.